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## RECONSTRUCTING INCOME STRATA IMPLICIT COALITIONS IN THE EU AND EFTA COUNTRIES

*The article, which aims to conduct a multi-criteria cluster analysis to classify countries by income distribution, growth, and implicit income coalition composition, allowed us to reconstruct implicit income coalitions that have benefited relatively more from economic growth. It also provided methodological advances by calculating right-wing policy indices and a centrist policy index to assess the actual social and economic policy regimes in advanced European economies. The highest right-wing policy indices were recorded in Bulgaria, the Netherlands, Poland, and Romania. The most left-wing policies were in Hungary, Greece, and Lithuania. The most centrist policies were recorded in Belgium, Croatia, and Slovakia. The highest policy polarization in favor of the richest and the poorest strata was identified in Germany and Italy. The type of policy implemented was found to have no significant impact on overall economic growth. On average, the strata in the coalition had 8 percentage points higher income growth over the analyzed 4-year period (2015-2019). This difference was generally larger in fast-growing economies. But the high correlation between the growth of coalition members and outsiders showed that outsiders also benefited significantly from economic growth, albeit to a lesser extent. With the exception of four countries outside the eurozone (Switzerland, Sweden, Norway, and Poland), economic growth was quite inclusive for outsiders and the poorest. A cluster analysis using several criteria allowed us to classify countries by income distribution, growth, and the implicit composition of the income coalition.*

**Key words:** income distribution, European countries, coalitions, economic policy, social policy, inequality, deciles, income growth, EU, EFTA, cluster analysis, economic growth, poverty, inclusion, inclusive development

## РЕКОНСТРУКЦІЯ НЕЯВИХ КОАЛІЦІЙ ЗА ДОХОДОМ У КРАЇНАХ ЄС ТА ЄАВТ

*Стаття, мета якої полягає у проведенні кластерного аналізу за запропонованими критеріями з метою оцінити і класифікувати країни ЄС і ЄАВТ на предмет розподілу доходів, зростання та неявного складу коаліції верств доходів, дозволила реконструювати неявні коаліції верств доходів, які отримали суттєву й відчутну вигоду від економічного зростання. У середині ЄС відбувається інституційна конвергенція, на що вказують індекс економічної свободи у широкому розумінні та індекс оцінки системи регулювання. Структурна конвергенція усередині ЄС не відбувається, натомість спеціалізація країн зберігається. Структурні відмінності між економіками ЦСЄ та центром ЄС майже вдвічі вищі, ніж у випадку південних чи скандинавських країн. Структурна дистанція між Півднем та Центром ЄС зараз така ж виразна, як і 1995 року – остання чверть століття не призвела до затребуваної конвергенції економіки ЄС розходяться з точки зору соціальної динаміки. Аналізовані показники соціального розвитку показують, що поляризація між Півднем і Північчю поглибилась. Кілька країн ЄС, зокрема на півдні, зазнали зростання матеріальних злиднів і безробіття (включаючи безробіття серед молоді), і зростаючий розрив у якості життя між поколіннями. В статті запропоновано альтернативні методологічні рішення для оцінки фактичних режимів соціальної та економічної політики у розвинених європейських економіках, зокрема, шляхом розрахунку індексів політики правого крила та індексу центристської політики. Проведений кластерний аналіз дозволив встановити, що найвищі індекси політики правого крила зафіксовані у Болгарії, Нідерландах, Польщі та Румунії. Найлівіша політика ідентифікована в Угорщині, Греції та Литві. Найбільш центристську політику зафіксовано у Бельгії, Хорватії та Словаччині. У Німеччині та Італії ідентифіковано найвищу поляризацію політики на користь найбагатіших і найбідніших верств. Було встановлено, що*

тин політики, що реалізується, не здійснює вирішального істотного впливу на загальне економічне зростання. У середньому верстви у коаліції мали на 8 п. п. більш вище зростання доходів за аналізований 4-річний період (2015-2019). Ця різниця, як правило, була вищою в швидкозростаючих економіках. Встановлена висока кореляція між зростанням членів коаліції та аутсайдерів підтверджує, що аутсайдери також суттєво виграють від економічного зростання, хоч і меншою мірою. За винятком 4 країн за межами Єврозони (Швейцарія, Швеція, Норвегія та Польща) економічне зростання було досить інклюзивним для аутсайдерів та найбільш бідних.

**Ключові слова:** розподіл доходів, європейські країни, коаліції, економічна політика, соціальна політика, нерівність, деціль, ЄС, ЄАВТ, Єврозона, кластерний аналіз, економічне зростання, бідність, інклюзія, інклюзивний розвиток

**JEL Classification:** D33, D72, E25, E65, O15

**Introduction.** Economic power is the ability to influence other actors, to master trends and resist external negative influences with economic means. It can be exercised at the international or intranational levels by various actors. Since each individual has a limited power, they tend to form coalitions, so that a coalition with the majority of power resources may provide relatively more favorable conditions for its members than for outsiders. At the formal political domain a coalition has to possess more than 50% of votes. At a company level shareholders who directly or indirectly control more than 50% votes make decisions. This is the very general framework of the necessary condition of existence of coalition, and the reality is much more complex. In reality 50% threshold is not a universal one. And decision making in the society involves many channels of influence (formal political institutions, companies, non-governmental organizations, informal communities etc.). Therefore we use the notion of implicit coalition where decision-making in various aspects of social, economic and political life is based on the common interests between its members unlike explicit coalition which is based on formal agreements. Reconstructing implicit coalitions may involve assessment of which strata benefit relatively more from the current state of affairs, i.e. increase disproportionately more their power resources relatively their power potential. This corresponds more to the concept of power in results unlike the concept power as potential. Income strata (such as the rich, the poor and the middle class) also can be treated as collective actors who themselves can form coalitions to promote their interests. The main aim of this paper is to determine which income strata form relatively more influential implicit coalitions in the EU and EFTA countries.

**Literature review.** Chugaiev O., Reznikova N., Bulatova O., Ptashchenko O., Ivashchenko O., Panchenko, V [1-3] studied the characteristics of intergenerational ties as a key factor in the formation of economic activity, and also noted the specific characteristics of the economic choice of representatives of different generations, which predetermines the political preferences of voters. Barro R. [4] has shown that the development of democratic institutions has a stimulating effect on economic growth at a low level of political freedom. As democracy expands, this effect decreases and becomes negative. In general, democracy has a weak negative effect on economic growth. Alessina A. and co-authors [5; 6] have established the absence of a relationship between the types of political regimes and the rates of economic growth. Stoetzer L. F., Giesecke J., Klüver H. [7], Traber D. [8], Turner T., D'Art D. [9], Engler S., Weisstanter D. [10], Schraff D., Pontusson J. [11], McKay L., Jennings W., Stoker G. [12] confirmed the thesis that the poorer the median voter in a society, the greater the demand he makes for the redistribution of income from the

rich to the poor in this society. This redistribution has a negative effect on economic growth for a number of reasons. The richer the individual, the higher his marginal propensity to save (the share of savings in income), all other things being equal, and, consequently, the lower the aggregate amount of savings in society - the level of capital accumulation - and, accordingly, the lower the investment and the rate of economic growth. The poorer the median voter in a democratic society, the greater the probability of expropriation for the rich members of this society. Accordingly, the fewer incentives economic agents have to invest: there is no point in investing in property that can be taken away at any time, and in a completely legal way. The poorer the median voter, the greater the demand he makes for redistribution and the higher the level of taxation. The overwhelming majority of actually applied taxes lead to an increase in prices for goods and services, which causes a reduction in demand and, accordingly, a reduction in social production and the welfare of society. All this influences the choice of political forces.

**Despite existing research** that shows that political institutions have an important, even determining, impact on the economic development of societies, as they structure the institutional environment and create incentives for individuals to supply different factors of production, specialize, and innovate, we aim to propose a methodological approach to classifying countries by income distribution, growth, and establishing their position relative to existing income coalitions.

**The purpose of the article** is to conduct a cluster analysis on several criteria in order to classify countries by income distribution, growth, and the implicit composition of the income coalition. This will allow us to establish whether economic growth has been sufficiently inclusive for outsiders and the poorest.

**Main results of the research.** The choice of the 27 EU and EFTA countries as the object of our analysis is based on the availability of statistics and the institutional development level associated with low shadow economy share which can distort income statistics. The source of data is Eurostat (2024) which publishes experimental statistics on Income and Living conditions (EU-SILC). Income strata in our study are deciles from the poorest D1 to the richest D10 in each individual country. The latest available data was for 2020, but the latter was an unusual period of the pandemic crisis. Therefore we used the growth rates in 2019 relatively 2015 as the base year. We assume that richer people have more resources to affect decision making de-facto unlike formal equality of votes under political voting. That's why an implicit coalition should include several deciles, which generate more than 50% of income. For examples, the richest 4 deciles may form a coalition themselves, but the poorest 4 deciles have to find allies

among other strata (medium class or alternatively even the rich people). An implicit coalition is defined as several deciles with highest growth rate of their income, so that they possess more than 50% of income. Other deciles are defined as outsiders, who benefit relatively less from the economic growth.

Then we calculate the shares of top 4 deciles (D7, D8,

$$RP_1 = TS - BS \quad (1)$$

and Centrist policy index (CP):

$$CP = MS + 0.5 - TS - BS \quad (2)$$

E.g. if the coalition contains D1, D4, D5 and D10, Right wing policy index (RP<sub>2</sub>) is calculated as: RP<sub>1</sub>=0.25-0.5 and CP=0.5+0.5-0.25-0.5. An alternative

$$RP_2 = \Sigma N/n \quad (3)$$

Where  $\Sigma N$  is the sum of the indices of deciles in the coalition and  $n$  is the quantity of deciles in the coalition.

E.g. in our previous example

$$RP_2 = (1 + 4 + 5 + 10)/4 \quad (4)$$

CV – coefficients of variation of income growth in all 10 deciles (standard deviation\*100%/ mean) was calculated to assess exclusiveness or inclusiveness of economic growth. We further consider or calculate several other indicators:

- D10/D1 – the ratio of income of the richest 10% and the poorest 10% of the population in 2015, times;
- IG – income (in euro) growth of the entire population in country in 2015-2019, %;
- IGD – the difference in average income growth of coalition (c) deciles and outsider (o) deciles in 2015-2019, p.p.

They were used for correlation analysis and k-means

D9, D10), middle 4 deciles (D4, D5, D6, D7) and bottom 4 deciles (D1, D2, D3, D4) which participate in the implicit coalition (denoted as TS, MS and BS respectively) to assess whether the coalition is relatively right, centrist or left. This ratios are used to calculate two indices: Right wing policy index (RP<sub>1</sub>):

cluster analysis of countries (the latter is based on standardized values to offset the difference in magnitude of values).

In the analyzed sample the top 3 deciles (D8-10) were the most frequent participants of coalitions (in 17-18 countries), followed by the middle 4 deciles (D4-7) which were members in 15-16 countries – see table 1. D1 and D2 were members in 13 countries. D3 was the least represented in coalitions (only in 11 countries), i.e. the moderately poor had usually the lowest income growth ratio. On average implicit coalition included 5.6 deciles (ranging from 3 in Bulgaria to 8 in Portugal) and earned 58% in come in a country (from 52.1% in Denmark to 71.2 in Austria).

Table 1

#### Implicit coalition attributes

Country	Deciles in coalition	TS	MS	BS	RP <sub>1</sub>	CP	RP <sub>2</sub>
Austria	1, 3-6, 9, 10	0.5	0.75	0.75	-0.25	0	5.4
Belgium	4-7, 10	0.5	1	0.25	0.25	0.75	6.4
Bulgaria	7, 9, 10	0.75	0.25	0	0.75	0	8.7
Croatia	5-7, 9 10	0.75	0.75	0	0.75	0.5	7.4
Cyprus	2, 4-9	0.75	1	0.5	0.25	0.25	5.9
Denmark	2, 7, 8, 10	0.75	0.25	0.25	0.5	-0.25	6.8
Estonia	3-6, 8, 9	0.5	0.75	0.5	0	0.25	5.8
Finland	1, 8-10	0.75	0	0.25	0.5	-0.5	7.0
Germany	1, 2, 8-10	0.75	0	0.5	0.25	-0.75	6.0
Greece	1- 5, 7, 8	0.5	0.75	1	-0.5	-0.25	4.3
Hungary	1-7	0.25	1	1	-0.75	0.25	4.0
Ireland	1-4, 6, 8, 10	0.5	0.5	1	-0.5	-0.5	4.9
Italy	1, 2, 8-10	0.75	0	0.5	0.25	-0.75	6.0
Latvia	2-4, 7, 8, 10	0.75	0.5	0.75	0	-0.5	5.7
Lithuania	1-6, 10	0.25	0.75	1	-0.75	0	4.4
Luxembourg	1, 5, 8-10	0.75	0.25	0.25	0.5	-0.25	6.6
Malta	3-5, 9-10	0.5	0.5	0.5	0	0	6.2
Netherlands	7-10	1	0.25	0	1	-0.25	8.5
Norway	3, 5, 7-9	0.75	0.5	0.25	0.5	0	6.4
Poland	6, 8-10	0.75	0.25	0	0.75	0	8.3
Portugal	1-8	0.5	1	1	-0.5	0	4.5
Romania	5, 7-10	1	0.5	0	1	0	7.8
Slovakia	1, 4-8	0.5	1	0.5	0	0.5	5.2
Slovenia	1, 2, 4, 6, 9, 10	0.5	0.5	0.75	-0.25	-0.25	5.3
Spain	1, 2, 4-8	0.5	1	0.75	-0.25	0.25	4.7
Sweden	2-6, 8, 9	0.5	0.75	0.75	-0.25	0	5.3
Switzerland	6, 7, 9, 10	0.75	0.5	0	0.75	0.25	8.0
Mean	-	0.63	0.56	0.48	0.15	-0.046	6.1

Source: authors' calculations based on Eurostat (2024)

At least 1 top-4decil was present in the coalition (D7 in Hungary and D10 in Lithuania). In the Netherlands and Bulgaria only the richest deciles formed the coalitions. No medium-4 deciles were coalition members in Finland, Germany and Italy. 6 countries had all medium-4 deciles in their coalitions. 6 countries had no bottom-4 deciles in the coalitions and 5 more had all the bottom-4 deciles in their coalitions. The highest right wing policy indices were in Bulgaria, the Netherlands, Poland, Switzerland, Romania and Croatia. The most leftish policy was in Hungary, Greece, Lithuania, Portugal, Spain and Ireland. The most centrist policy was in Belgium, Croatia, Slovakia and to lower extent Cyprus, Estonia, Hungary, Spain and Switzerland. The most polarized policy (favoring the richest and the poorest) was in Germany, Italy, Finland, Ireland and Latvia.

Table 1 shows original income inequality in the countries and income trends. On average the richest 10% of the population earned 8 times more than the poorest 10%. The highest inequality was in the Balticstates and Germany and

the lowest one was in Slovakia, Hungary, Malta, Poland, Belgium and Slovenia. The fastest growing economies included Hungary, Romania, Ireland, Lithuania and Bulgaria. The slowest economies were Switzerland, Sweden and Norway. These both groups included mostly countries outside the Euro area, therefore exchange rate changes could affect the results. The average difference in income growth of coalition members and outsiders was 8.5 p.p. (table 2). The difference was usually higher in fast growing economies especially in Hungary. But it was also high in slower growing economies of Poland and Luxemburg. The smallest difference was in Romania (despite it was a fast growing economy), Slovenia, Austria, Belgium and Croatia. Switzerland was the only country where outsider's income growth was negative. Coefficient of variation of income growth for all the deciles was the highest in Switzerland (due to negative income growth in the bottom-4 deciles) followed by Poland (bottom-3 deciles), Norway and Sweden (D1)

Table 2

## Income inequality and income growth

Country	D10/D1	IG	IGc	IGo	IGD	CV
Austria	6.8	15.5	16.7	13.3	3.4	18
Belgium	5.7	17.5	19.6	15.9	3.7	14
Bulgaria	9.4	45.5	47.4	35.8	11.6	24
Croatia	9.2	27.4	28.6	24.2	4.4	11
Cyprus	6.5	24.7	28.5	19.3	9.2	20
Denmark	9.6	10.9	13.6	8.2	5.4	50
Estonia	10.2	32.9	38.2	26.0	12.2	23
Finland	7.2	12.5	15.7	9.2	6.5	34
Germany	11.5	26.2	29.2	22.2	7.1	18
Greece	7.2	12.8	17.0	9.9	7.1	43
Hungary	5.2	65.2	75.4	56.8	18.6	18
Ireland	6.2	52.5	59.4	46.1	13.3	17
Italy	8.8	9.8	12.7	8.2	4.5	41
Latvia	12.1	38.6	44.3	35.4	8.9	16
Lithuania	11.3	48.0	55.9	40.2	15.8	16
Luxembourg	8.7	17.3	26.0	11.4	14.6	70
Malta	5.3	39.2	42.3	29.5	12.8	34
Netherlands	7.0	20.9	22.4	16.5	5.9	24
Norway	9.0	6.4	8.4	1.8	6.6	97
Poland	5.4	11.9	16.6	2.4	14.2	136
Portugal	9.1	18.9	24.6	13.3	11.3	28
Romania	8.5	63.8	56.9	54.4	2.4	14
Slovakia	4.8	23.6	26.3	17.5	8.8	36
Slovenia	5.7	21.6	21.1	18.6	2.5	17
Spain	7.6	17.6	21.7	14.0	7.7	24
Sweden	7.5	3.6	5.7	0.1	5.7	74
Switzerland	7.4	3.4	4.9	-0.8	5.7	294
Mean	7.9	25.5	28.9	20.4	8.5	

Source: authors' calculations based on Eurostat (2024)

The correlation analysis shows that centrist policy is less likely to be in countries with high inequality (correlation between CP and D10/D1 is -0.37,  $p < 0.1$ ). The difference in average income growth of coalition deciles and outsider deciles is higher in fast growing economies (correlation between IG and IGD is 0.46,  $p < 0.05$ ). But other considered indicators are not significantly correlated with economic growth (there is insignificant negative correlation -0.21 between right wing policy index  $RP_1$  and income growth IG). Despite the difference between coalition members' and outsiders' income growth, correlation between them is very high and significant 0.97 ( $p < 0.01$ ). This shows that the policy of a coalition in a typical advanced European country is rather inclusive than exclusive. The

difference between coalition members' and outsiders' income growth is smaller under right wing policy (the correlation between  $RP_1$  and IGD is -0.38,  $p < 0.1$ ), although the effect can be rather associated with the correlations between IGD and IG and between IG and  $RP_1$ . Table 3 shows results of clusterization based on representation of top, middle and bottom deciles in the coalitions. Cluster 1 is moderate leftish. Cluster 2 is mainly right wing with a minor centrist component. Cluster 3 is right wing with a minor leftish component. Cluster 4 is the most inclusive, where all strata are equally represented in the coalition. Cluster 5 is the most centrist with a minor right wing component.

Table 3

Cluster analysis results for income strata composition of an implicit coalition

	Cluster 1	Cluster 2	Cluster 3	Cluster 4	Cluster 5
Mean TS	0.44	0.81	0.75	0.58	0.63
Mean MS	0.81	0.34	0.00	0.56	0.94
Mean BS	0.91	0.09	0.42	0.60	0.31
Cluster members	Austria, Greece, Hungary, Ireland, Lithuania, Portugal, Spain, Sweden	Bulgaria, Denmark, Luxemburg, the Netherlands, Norway, Poland, Romania, Switzerland	Finland, Germany, Italy	Estonia, Latvia, Malta, Slovenia, the EU average	Belgium, Croatia, Cyprus, Slovakia

Source: authors' calculations based on Eurostat (2024)

Table 4 shows results of clusterization based on initial income distribution in 2015, overall income growth and changes in income distribution in 2015-2019. Cluster 1 is with an average income inequality, small economic growth and right wing policy. Cluster 2 included countries with

high inequality, fast enough income growth and centrist policy. Cluster 3 tended to have low inequality, the fastest economic growth and leftish policy. Cluster 4 has lower than average inequality, relatively slow income growth and leftish policy.

Table 4

Cluster analysis results for income distribution and growth

	Cluster 1	Cluster 2	Cluster 3	Cluster 4
Mean D10/D1	7.9	10.3	5.5	6.9
Mean IG	11.6	40.4	52.3	18.1
Mean $RP_2$	7.2	6.5	5.0	5.3
Cluster members	Denmark, Finland, Italy, Luxemburg, the Netherlands, Norway, Poland, Switzerland	Bulgaria, Croatia, Estonia, Germany, Latvia, Lithuania, Romania	Hungary, Ireland, Malta	Austria, Belgium, Cyprus, Greece, Portugal, Slovakia, Slovenia, Spain, Sweden, the EU average

Source: authors' calculations based on Eurostat (2024)

**Conclusion.** When assessing the performance of governments, voters usually look at inflation, unemployment, and possibly output growth. Experienced citizens, concerned about current and future welfare, can assess what combinations of unemployment and inflation were actually possible in different periods and, on this basis, determine their level of satisfaction with the policies implemented in the country. Some seek a formula for "optimal" policy by trying to compare the macroeconomic results of the government's actual policy choices with the indicators that could potentially have been possible if more successful

measures had been taken. Politicians, having the opportunity to conduct sovereign policy, are in a constant choice. If the current government adjusts monetary and fiscal policy so that the actual level of output is maintained above the natural rate (and unemployment is kept below the natural rate), then this will ultimately accelerate inflation. If the level of output is maintained below the natural rate (and in this case unemployment is kept above the natural rate), then the rate of inflation will decrease. The fact of life is that if the output of a given country is equal to the highest level of the country's GDP that can be generated given the

existing labor, natural resources, and technology at society's disposal, then a certain level of inflation can be maintained indefinitely. The problem is that voters do not perceive inflation, but are ready to sing the praises of increased productivity or low unemployment. This means that voters who understand the above-mentioned long-run and short-run relationships would evaluate politicians differently. The inflation recorded today is largely determined by past inflation expectations, which are not easily controlled by current policy decisions. Expected inflation may be the result of the mistakes of past politicians, and experienced voters will not punish the current government for the shortcomings of its predecessors.

Experienced voters may also be reluctant to seek higher real GDP, since its higher-than-natural level causes faster inflation, and thus the depreciation of savings. That is, experienced voters recognize that short-term policy choices are limited to the choice between unemployment and inflation, and they will reward or punish politicians depending on whether the tradeoff they choose helps them achieve their desired long-term outcomes. True, life sometimes throws up an unpleasant surprise in the form of stagflation—a situation in which prices and unemployment rise simultaneously. The paper enabled to reconstruct implicit

coalitions of income strata, which benefited relatively more from economic growth. It also provided methodological advances by calculating right wing policy indices and centrist policy index to assess de-facto modes of social and economic policies in the advanced European economies. The highest right wing policy indices were in Bulgaria, the Netherlands, Poland and Romania. The most leftist policy was in Hungary, Greece and Lithuania. The most centrist policy was in Belgium, Croatia and Slovakia. In Germany and Italy was the highest policy polarization favoring the richest and the poorest strata. Type of policy does not significantly affect overall economic growth. The strata in a coalition on average had 8 p.p. higher income growth in the analyzed 4 year period (2015-2019). This difference tended to be higher in fast growing economies. But high correlation between coalition members' and outsiders' growth showed that outsiders also benefit substantially from economic growth, although at lower extent. Except for 4 countries outside the Euro Area (Switzerland, Sweden, Norway and Poland) the economic growth was inclusive enough for outsiders and the poorest as well. Cluster analysis according to multiple criteria allowed to classify countries according to their income distribution, growth and implicit income strata coalition composition.

#### Список використаних джерел:

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